# Quarterly Commentary: Fixed Income Funds

**March 31, 2019**

| | |
|---|---|
| **Short Duration Total Return Fund** | **Corporate Credit Fund** |
| **Core Bond Fund** | **High Yield Fund** |

## Our Mission

At Diamond Hill, ***we serve*** our clients by providing investment strategies that deliver lasting value through a shared commitment to our intrinsic value-based investment philosophy, long-term perspective, disciplined approach and alignment with our clients' interests.

### VALUE

***We believe*** market price and intrinsic value are independent in the short-term but tend to converge over time.

### LONG-TERM

***We maintain*** a long-term focus both in investment analysis and management of our business.

### DISCIPLINE

***We invest*** with discipline to increase potential return and protect capital.

### PARTNERSHIP

***We align*** our interests with those of our clients through significant personal investment in our strategies.

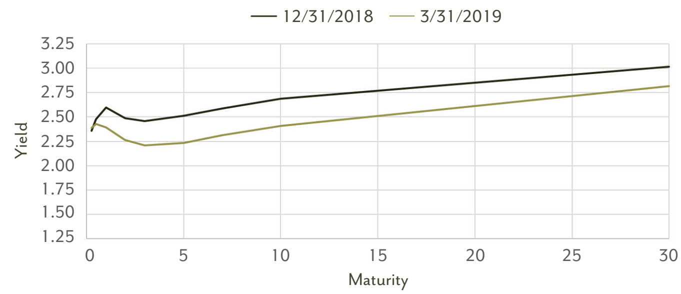
# First Quarter 2019 Review: Fixed Income Markets

As of March 31, 2019

Continuing the dominance exhibited in the fourth quarter, the Federal Open Market Committee (FOMC) remained firmly in the driver's seat regarding market volatility, relegating geopolitical uncertainties like the U.S.-China trade war and the ongoing drama of Brexit to second-tier importance. Following up on the roughly received press conference at the end of 2018, Jerome Powell gathered with his predecessors Janet Yellen and Ben Bernanke in Atlanta to begin the process of walking back comments from the fourth quarter. Balance sheet flexibility and "the utilization of all tools" to orchestrate a soft landing were prevalent themes, and the FOMC utilized both the January 30 and March 20 meetings to transition from a slightly hawkish to fully dovish posture in the span of a few months. The quarterly Dot Plot clearly outlined the outlook shift from the various members of the FOMC, moving from one to two rate increases in 2019 and one increase in 2020 to zero rate increases in 2019 and one increase in 2020. Powell also introduced the notion of balance sheet tapering in 2019 at the January meeting, solidifying the process at the March 20 meeting. Fixed income assets across the spectrum responded strongly, delivering strong absolute returns. Treasuries delivered over 2% during the first quarter, as investment grade corporate debt experienced its best first quarter since 1995 and best overall quarter since 2009. The securitized market returned 2.22% while the ICE BofA ML U.S. High Yield Index returned 7.40%, its best first quarter return since 1992.

*Treasury*

On the heels of its strongest quarter since early 2016, the 10-year Treasury delivered a 3.08% return during the first quarter of 2019. While the curve moved lower across all maturities (except for the 3-month Treasury), the biggest impact was felt on the longer end of the curve, with the 30-year Treasury generating a 4.98% return during the quarter as the yield moved from 3.01% to 2.81%, the largest quarterly drop since the second quarter of 2016. Maturities from 1-year to 30-year declined 24.5 bps on average, with the 10-year Treasury declining most significantly, down 27.9 bps during the quarter. For maturities less than one year, there was minimal movement in yield, as the average quarter-over-quarter change in yields was less than one basis point. The 6-month Treasury declined 5.3 bps during the quarter, while the 3-month Treasury increased 2.6 bps, and the 1-month Treasury was essentially unchanged.




| | 3-MO | 6-MO | 1-YR | 2-YR | 3-YR | 5-YR | 7-YR | 10-YR | 30-YR |
|---|---|---|---|---|---|---|---|---|---|
| **12/31/18** | 2.35 | 2.47 | 2.60 | 2.49 | 2.46 | 2.51 | 2.59 | 2.69 | 3.01 |
| **3/31/19** | 2.39 | 2.42 | 2.39 | 2.26 | 2.21 | 2.23 | 2.31 | 2.41 | 2.81 |
| **Change** | 0.03 | -0.05 | -0.21 | -0.23 | -0.25 | -0.28 | -0.27 | -0.28 | -0.20 |

*Securitized*

While the investment grade sector experienced one of the strongest quarters in recent memory, the securitized market continued to deliver consistent absolute returns. Commercial mortgage-backed securities (CMBS) delivered the strongest performance during the quarter with a 3.24% return, followed by residential mortgage-backed securities (RMBS), and asset-backed securities (ABS), which returned 2.17% and 1.48%, respectively. Relative to comparable-duration Treasuries, which delivered strong returns during the quarter, the securitized market held up well. CMBS delivered 118 bps of excess return, ABS delivered 40 bps of excess return, and RMBS delivered 28 bps of excess return. Within the ABS sector, autos returned 1.44% (43 bps excess return) and credit cards returned 1.49% (37 bps excess return).

*Investment Grade and High Yield Credit*

Rebounding from the fourth quarter's negative performance, the Bloomberg Barclays U.S. Corporate Index delivered its best quarterly return (5.14%) since the second quarter of 2009. Index performance was led by the industrials sector, which returned 5.50% (295 bps excess return), while financials (4.61%, 257 bps excess return) and utilities (4.57%, 156 bps excess return) delivered positive performance as well. The risk-on trade during the first quarter drove performance across the investment grade corporate sector. The high yield portion of the U.S. corporate bond market, as represented by the ICE BofA ML U.S. High Yield Index, began the year with a yield to worst (YTW) of 7.95% and an option-adjusted spread (OAS) of 533 bps. After generating a 7.40% total return during the first quarter, the High Yield Index ended the quarter with a 6.48% YTW and OAS of 405 bps. The strong first quarter return for the High Yield Index more than offset the -4.67% return in the fourth quarter of last year, providing another example of the resilience of the high yield asset class. Over the last two quarters, the High Yield Index has returned 2.40%, while the S&P 500 Index and Russell 2000 Index have declined 1.72% and 8.56%, respectively.

*All Fund returns based on Class I shares.*

The Fund generated a 1.46% total return during the first quarter, compared to 1.21% for the Bloomberg Barclays U.S. 1-3 Year Government/Credit Index. Since its inception on July 5, 2016, the Fund has generated a total return of 3.75% compared to 1.17% for the Index. The goal of the Diamond Hill Short Duration Total Return Fund is to outperform the Index over a market cycle, while generating a yield and return advantage relative to the benchmark. We are pleased with how the Fund has performed on a relative basis both during the most recent quarter and since inception.

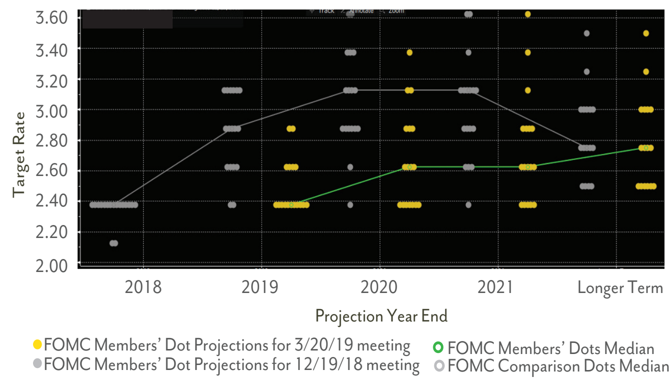
Continuing the dominance exhibited in the fourth quarter, the Federal Open Market Committee (FOMC) remained firmly in the driver's seat regarding market volatility, relegating geopolitical uncertainties like the U.S.-China trade war and the ongoing drama of Brexit to second-tier importance. Following up on the roughly received press conference at the end of 2018, Jerome Powell gathered with his predecessors Janet Yellen and Ben Bernanke in Atlanta to begin the process of walking back comments from the previous quarter. Balance sheet flexibility and "the utilization of all tools" to orchestrate a soft landing were the themes of the day and the FOMC utilized both the January 30 meeting and the March 20 meeting to transition from a slightly hawkish posture to fully dovish in the span of a few months. The quarterly published Dot Plot clearly outlined the shift in outlook from the various members of the FOMC by moving from one or two rate increases in 2019 and one increase in 2020 to no rate increases in 2019 and one increase in 2020. Powell also introduced the notion of balance sheet tapering in 2019 at the January meeting and then solidified the process in the March meeting.

Fixed income assets across the spectrum responded strongly, delivering strong absolute returns. Treasuries delivered over 2% during the first quarter, as investment grade corporate debt experienced its best first quarter since 1995 and best overall quarter since 2009. The securitized market returned 2.22% while the ICE BofA ML U.S. High Yield Index returned 7.40%, its best first quarter return since 1992.

## TEAM

| | |
|---|---|
| **Mark Jackson, CFA**<br>Portfolio Manager | **Henry Song, CFA**<br>Portfolio Manager |
| **Douglas Gimple**<br>Senior Portfolio Specialist | |

## IMPLIED FED FUNDS TARGET RATE




Source: Bloomberg.

Fueled by the dovish pivot by the Federal Reserve, the yield curve shifted dramatically lower across all maturities with the biggest impact felt on the longer end of the curve. The shift in rate outlook from the Fed, as outlined in the Dot Plot released in March as well as from comments by Fed Chair Powell, reinforced the notion of a "pause." Immediately following the FOMC press conference on March 20, the 3-month Treasury bill and the 10-year Treasury bond inverted and remained in that position for four days before reverting to a more normalized but incredibly tight relationship. During the quarter, the 3-month Treasury bill barely moved, from 2.36% to 2.38%, while the 10-year Treasury dropped from 2.68% to 2.41%. During the month of March, the 10-year Treasury dropped from 2.72% to 2.41%, which was the largest one-month drop in yield since the early days of Brexit in June 2016.

It is important to note that the Short Duration Total Return Fund works to provide yield for investors while focusing on the shorter end of the fixed income markets. Though there is a concentration on the shorter end of the yield curve, the Fund maintains a certain level of interest rate risk and can experience some price volatility in uncertain markets. We believe there are opportunities to add incremental yield over the benchmark by investing in structured product across the quality spectrum. The Fund strives to maintain an average credit quality rating of A while taking advantage of mispriced opportunities in both unrated securities and a small allocation to below investment grade securities.

As of March 31, 2019, the Fund had a yield to worst (YTW) of 4.00% with an effective duration of 1.32, compared to the Index's YTW of 2.45% and effective duration of 1.91. Asset-backed securities (ABS) remain the largest allocation in the Fund and was the strongest contributor to the yield advantage of the portfolio over the benchmark.

Within the securitized sector, ABS delivered strong performance led by consumer and auto loans. Residential and commercial mortgage-backed securities also contributed to relative performance during the quarter. The Fund's underweight position in the corporate sector relative to the benchmark detracted slightly from performance as the short end of the corporate sector delivered strong returns during the quarter.

Despite an increase in the Fund's Treasury allocation, the underweight relative to the index detracted from relative performance as the Bloomberg Barclays U.S. 1-3 Year Treasury Index (a component of the Bloomberg Barclays U.S. 1-3 Year Government / Corporate Index) delivered 88 bps of return as rates rallied across the curve.

The Fund continues to search for opportunities in the marketplace while maintaining an attractive yield relative to the benchmark.

## PERIOD AND AVERAGE ANNUAL TOTAL RETURNS AS OF MARCH 31, 2019

| | SINCE INCEPTION (7/5/16) | 1-YR | YTD | 1Q19 | EXPENSE RATIO |
|---|---|---|---|---|---|
| RETURNS AT NAV (WITHOUT SALES CHARGE) | | | | | |
| **Class I** | 3.75% | 4.08% | 1.46% | 1.46% | 0.52% |
| BENCHMARK | | | | | |
| **Bloomberg Barclays U.S. 1-3 Yr. Gov./Credit Index** | 1.17 | 3.03 | 1.21 | 1.21 | — |

Must be preceded or accompanied by a prospectus.

***Risk Disclosure:*** The value of fixed-income securities varies inversely with interest rates; as interest rates rise, the market value of fixed-income securities will decline. Lower quality debt (ie: "High Yield") securities involve greater risk of default or price changes due to potential changes in the issuer's credit quality. The value of investments in mortgage-related and asset-backed securities will be influenced by the factors affecting the housing market and the assets underlying such securities. The securities may decline in value, face valuation difficulties, become more volatile and/or become illiquid. They are also subject to prepayment risk, which occurs when mortgage holders refinance or otherwise repay their loans sooner than expected, creating an early return of principal to holders of the loans.

The views expressed are those of the portfolio managers as of March 31, 2019, are subject to change and may differ from the views of other portfolio managers or the firm as a whole. These opinions are not intended to be a forecast of future events, a guarantee of results, or investment advice.

***The performance data quoted represents past performance; past performance does not guarantee future results.*** *The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. The Fund's current performance may be lower or higher than the performance data quoted. Investors may obtain performance information current to the most recent month-end, within 7 business days, at diamond-hill.com.*

Performance returns assume reinvestment of all distributions. Returns for periods less than one year are not annualized.

Fund holdings subject to change without notice.

The Bloomberg Barclays U.S. 1-3 Yr. Gov./Credit Index is an unmanaged index of investment grade government and corporate bonds with maturities of one to three years.This index does not incur fees and expenses (which would lower the return) and is not available for direct investment.

Analytics provided by The Yield Book® Software.

***An investor should consider the Fund's investment objectives, risks, and charges and expenses carefully before investing or sending any money. This and other important information about the Fund(s) can be found in the Fund's(s) prospectus or summary prospectus which can be obtained at diamond-hill.com or by calling 888.226.5595. Please read the prospectus or summary prospectus carefully before investing. The Diamond Hill Funds are distributed by Foreside Financial Services, LLC (Member FINRA). Diamond Hill Capital Management, Inc., a registered investment adviser, serves as Investment Adviser to the Diamond Hill Funds and is paid a fee for its services. Like all mutual funds, Diamond Hill Funds are not FDIC insured, may lose value, and have no bank guarantee.***

# Diamond Hill Core Bond Fund Commentary

As of March 31, 2019

*All Fund returns based on Class I shares.*

The Fund generated a 2.66% total return during the first quarter, compared to 2.94% for the Bloomberg Barclays U.S. Aggregate Index. Since its inception on July 5, 2016, the Fund has generated a total return of 2.26% compared to 1.15% for the Index. The goal of the Diamond Hill Core Bond Fund is to outperform the Index over a market cycle. Though it underperformed during the most recent quarter, the Core Bond Fund has delivered strong relative performance since inception.

Continuing the dominance exhibited in the fourth quarter, the Federal Open Market Committee (FOMC) remained firmly in the driver's seat regarding market volatility, relegating geopolitical uncertainties like the U.S.-China trade war and the ongoing drama of Brexit to second-tier importance. Following up on the roughly received press conference at the end of 2018, Jerome Powell gathered with his predecessors Janet Yellen and Ben Bernanke in Atlanta to begin the process of walking back comments from the previous quarter. Balance sheet flexibility and "the utilization of all tools" to orchestrate a soft landing were the themes of the day and the FOMC utilized both the January 30 meeting and the March 20 meeting to transition from a slightly hawkish posture to fully dovish in the span of a few months. The quarterly published Dot Plot clearly outlined the shift in outlook from the various members of the FOMC by moving from one or two rate increases in 2019 and one increase in 2020 to no rate increases in 2019 and one increase in 2020. Powell also introduced the notion of balance sheet tapering in 2019 at the January meeting and then solidified the process in the March meeting.

Fixed income assets across the spectrum responded strongly, delivering strong absolute returns. Treasuries delivered over 2% during the first quarter, as investment grade corporate debt experienced its best first quarter since 1995 and best overall quarter since 2009. The securitized market returned 2.22% while the ICE BofA ML U.S. High Yield Index returned 7.40%, its best first quarter return since 1992.

Fueled by the dovish pivot by the Federal Reserve, the yield curve shifted dramatically lower across all maturities with the biggest impact felt on the longer end of the curve. The shift in rate outlook from the Fed, as outlined in the Dot Plot released in March as well as from comments by Fed Chair Powell, reinforced the notion of a

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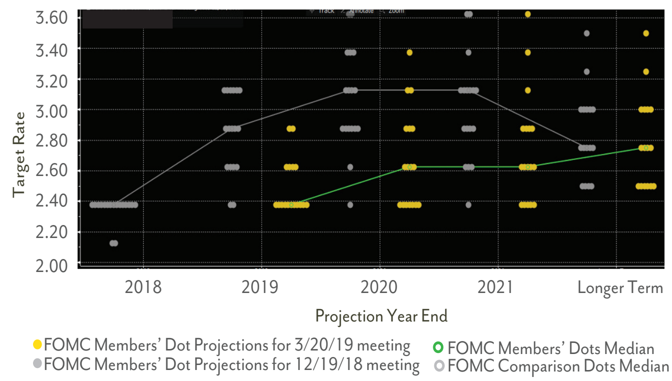
Senior Portfolio Specialist

## IMPLIED FED FUNDS TARGET RATE




Source: Bloomberg.

"pause." Immediately following the FOMC press conference on March 20, the 3-month Treasury bill and the 10-year Treasury bond inverted and remained in that position for four days before reverting to a more normalized but incredibly tight relationship. During the quarter the 3-month Treasury bill barely moved, from 2.36% to 2.38%, while the 10-year Treasury dropped from 2.68% to 2.41%. During the month of March, the 10-year Treasury dropped from 2.72% to 2.41%, which was the largest one-month drop in yield since the early days of Brexit in June 2016.

Following on the heels of its strongest quarter since early 2016, the 10-year Treasury delivered 3.08% in the first quarter of 2019. While the curve moved lower across all maturities (except for the 3-month Treasury bill), the biggest impact was felt on the longer end of the curve, with the 30-year Treasury generating 4.98% return during the quarter as the yield moved from 3.01% to 2.81%, the largest quarterly drop since the second quarter of 2016. Maturities from 1-year to 30-year declined an average of 24.5 bps with the largest move occurring with the 10-year Treasury declining 27.9 bps. For maturities less than one year, there was minimal movement as the average change quarter over quarter was less than one basis point, with the 6-month Treasury declining by 5.3 bps while the 3-month increased 2.6 bps and the 1-month was essentially unchanged. The Fund maintained an underweight to Treasuries relative to the index (20.06% v. 38.8%) but the longer duration posture of the Fund's holdings contributed to performance during the quarter.

The Fund's duration has been maintained within our targeted range of +/-10% of the benchmark's duration. At the end of the first quarter, the Fund's duration was 5.26 compared to the index duration of 5.82, reflecting the long-term viewpoint that interest rates have a greater chance of moving higher over the coming months and quarters. Rates rallied throughout the quarter, pushing the duration of the Bloomberg Barclays U.S. Aggregate Index to 5.82 at the end of the first quarter from year end 2018 level of 5.87. The Fund's overall shorter duration positioning relative to the benchmark detracted from performance during the quarter.

Rebounding from the previous quarter's negative performance, the Bloomberg Barclays U.S. Corporate Index delivered its best quarterly return (5.14%) since the second quarter of 2009. The Index was powered by the industrial sector, which returned 5.50% (295 bps excess return) while financials (4.61%, 257 bps excess) and utilities (4.57%, 156 bps excess) helped to drive the Index performance during the quarter. The risk-on trade during the first quarter pushed the strong returns across the investment grade corporate sector. The Fund's positioning in its corporate allocation detracted from performance as a result of the significant underweight in industrials and utilities and the shorter duration positioning in financials.

While the investment grade sector experienced one of the strongest quarters in recent memory, the securitized market continued to deliver consistent absolute returns. Commercial mortgage-backed securities (CMBS) delivered the strongest performance during the quarter, with 3.24% return, followed by residential mortgage-backed securities (RMBS) with 2.17% return and asset-backed securities (ABS) returning 1.48%. Relative to comparable duration Treasuries, which delivered strong performance during the quarter, the securitized market held up well. CMBS delivered 118 bps of excess return, ABS 40 bps of excess return and RMBS 28 bps of excess return. Within the ABS sector, autos returned 1.44% (43 bps excess return) and credit cards returned 1.49% (37 bps excess return). The Fund's overweight in the securitized sector contributed to performance during the quarter, with CMBS delivering the strongest contribution.

The Fund continues to search for opportunities in the marketplace while maintaining a conservative risk profile relative to the Index.

## PERIOD AND AVERAGE ANNUAL TOTAL RETURNS AS OF MARCH 31, 2019

| | SINCE INCEPTION (7/5/16) | 1-YR | YTD | 1Q19 | EXPENSE RATIO |
|---|---|---|---|---|---|
| RETURNS AT NAV (WITHOUT SALES CHARGE) | | | | | |
| **Class I** | 2.26% | 5.17% | 2.66% | 2.66% | 0.47% |
| BENCHMARK | | | | | |
| **Bloomberg Barclays U.S. Aggregate Index** | 1.15 | 4.48 | 2.94 | 2.94 | — |

Excess return indicates the return over comparable duration Treasuries.

***Risk Disclosure:*** The value of fixed-income securities varies inversely with interest rates; as interest rates rise, the market value of fixed-income securities will decline. Lower quality debt (ie: "High Yield") securities involve greater risk of default or price changes due to potential changes in the issuer's credit quality. The value of investments in mortgage-related and asset-backed securities will be influenced by the factors affecting the housing market and the assets underlying such securities. The securities may decline in value, face valuation difficulties, become more volatile and/or become illiquid. They are also subject to prepayment risk, which occurs when mortgage holders refinance or otherwise repay their loans sooner than expected, creating an early return of principal to holders of the loans.

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Performance returns assume reinvestment of all distributions. Returns for periods less than one year are not annualized. Class I shares have no sales charge.

Fund holdings subject to change without notice.

The Bloomberg Barclays U.S. Aggregate Index is an unmanaged index representing the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through, and asset-backed securities. The Bloomberg Barclays U.S. Corporate Index is an unmanaged index measuring the investment grade, fixed-rate, taxable corporate bond market. It includes USD Denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers. These indices do not incur fees and expenses (which would lower the return) and are not available for direct investment.

Analytics provided by The Yield Book® Software.

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# Diamond Hill Corporate Credit Fund Commentary

As of March 31, 2019

*All Fund returns based on Class I shares.*

The Fund generated a 5.64% total return during the first quarter compared to 5.38% for the ICE BofA ML U.S. Corporate & High Yield Index. For the trailing five years, the Fund generated an annualized total return of 5.63% compared to 3.88% for the Corporate & High Yield Index.

Unlike most corporate bond funds, the Diamond Hill Corporate Credit Fund is not managed against any index. Instead, the Fund is managed against absolute objectives within a range of inflation plus 3% and 7% nominal, each measured over rolling five-year periods. Our goal is to generate a yield and total return within that range while minimizing the risk of downside volatility over longer time periods. Although the Fund's investable universe (and the Corporate & High Yield Index) includes both investment grade and high yield corporate bonds, since early 2010 the Fund has been largely focused on the high yield portion of the market to achieve these objectives. About 78% of the Fund was in high yield corporate bonds at the end of the fourth quarter.

The high yield portion of the U.S. corporate bond market, as represented by the ICE BofA ML U.S. High Yield Index, began the year with a yield to worst (YTW) of 7.95% and an option-adjusted spread (OAS) of 533 bps. After generating a 7.40% total return for the quarter, the High Yield Index ended the quarter with a 6.48% YTW and OAS of 405 bps. The strong return for the High Yield Index more than offset the -4.67% return in the fourth quarter of last year. This is another example of the resilience of the high yield asset class. Over the last two quarters, the High Yield Index generated a 2.39% return while the S&P 500 was -1.72% and the Russell 2000 was -8.56%.

We want to hold up better than peers in down markets and then capture our fair share of the upside in strong markets. This should allow us to achieve our objectives and generate competitive returns over a complete market cycle. While we typically focus on much longer time periods, the last two quarters are instructive because they represent a mini-cycle over which we tracked our long-term objectives. Our performance compared to peers in the Morningstar High Yield Category was strong in the fourth quarter of last year and then weak in the first quarter of this year. But, over both quarters, the Fund was in the 8th percentile of the category. Compared to the High Yield Index, the Fund captured only 48% of the downside in the fourth quarter and then 76% of the upside in the first quarter. For the six-month period, the Fund generated a positive 3.29% return, which was 90 bps better than the 2.39% return of the High Yield Index. While the beginning of the fourth quarter seemed like a horrible time to invest in high yield, we are pleased with the Fund's absolute return over this six-month period.

## TEAM


**Bill Zox, CFA**
Portfolio Manager

**John McClain, CFA**
Portfolio Manager

**Suken Patel, CFA**
Assistant Portfolio Manager

**Douglas Gimple**
Senior Portfolio Specialist


Last quarter, we wrote about an 18 percentage point increase in the Fund's exposure to BB-rated bonds during 2018 as Treasury yields increased and credit spreads widened. Treasury yields declined and credit spreads narrowed dramatically in the first quarter and BB-rated bonds benefited from both. As the price of BB-rated bonds approached our estimates of intrinsic value, we reduced the Fund's BB weighting by 10 percentage points in favor of a higher cash position and a higher weighting in BBB-rated bonds. High yield investors were moving up in credit quality which made BB-rated bonds more expensive. Investment grade investors were also moving up in credit quality which made certain BBB-rated bonds attractive, particularly compared to BB-rated bonds. In addition, while interest rates remain low, we are, at the margin, willing to bear more interest rate risk relative to credit risk at this stage of the cycle. Because the Fund is not managed against any benchmark, we are happy to swap BB exposure for BBB exposure if that is where valuations lead us.

The Fund's YTW is typically somewhere in the range of our absolute objectives, although it was well below the low end of the range in late June 2014 and well above the high end of the range in early February 2016. At the end of the quarter, the Fund's YTW was 5.12%. The Fund's duration was 3.13, within the typical 2.0-3.5 range and below the High Yield Index duration of 3.69 and the Corporate & High Yield Index duration of 6.65.

The Federal Reserve spent most of 2018 trying to get out of the business of suppressing volatility in financial assets. After risk assets started to buckle in the fourth quarter, the Fed realized that financial conditions were unnecessarily tight and the Fed shifted to a much more dovish stance. While volatility in both bonds and stocks has come down far more than we expected, we are confident that it will come back as is typical later in the economic and market cycles. We want to be in a strong position to take advantage of that volatility. As always, we are focused on delivering risk-adjusted returns over a complete market cycle by holding up better during down markets and capturing our fair share of up markets.

## PERIOD AND AVERAGE ANNUAL TOTAL RETURNS AS OF MARCH 31, 2019

| | SINCE INCEPTION (9/30/02) | 10-YR | 5-YR | 3-YR | 1-YR | YTD | 1Q19 | EXPENSE RATIO GROSS | NET[1] |
|---|---|---|---|---|---|---|---|---|---|
| RETURNS AT NAV (WITHOUT SALES CHARGE) | | | | | | | | | |
| **Class I** | 7.11% | 9.61% | 5.63% | 7.88% | 5.97% | 5.64% | 5.64% | 0.64% | 0.63% |
| BENCHMARK | | | | | | | | | |
| **ICE BofAML U.S. Corporate & High Yield Index** | 5.96 | 7.61 | 3.88 | 4.57 | 5.13 | 5.38 | 5.38 | — | — |

Must be preceded or accompanied by a prospectus.

[1] The Fund may invest in another Diamond Hill Fund. Diamond Hill Capital Management, Inc. is required to permanently waive a portion of its management fee in the pro-rata amount of the management fee charged by the underlying Diamond Hill Fund.

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Performance returns assume reinvestment of all distributions. Returns for periods less than one year are not annualized. Class I shares include Class A share performance achieved prior to the creation of Class I shares. Class I shares have no sales charge.

Fund holdings subject to change without notice.

The ICE BofA Merrill Lynch U.S. Corporate & High Yield Index is comprised of U.S. dollar denominated investment grade and below investment grade corporate debt publicly issued in the U.S. domestic market. The ICE BofA Merrill Lynch U.S. High Yield Index tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market.

The index data referenced herein is the property of ICE Data Indices, LLC, its affiliates ("ICE Data") and/or its third party suppliers and has been licensed for use by Diamond Hill Capital Management, Inc. ICE Data and its third party suppliers accept no liability in connection with its use. See diamond-hill.com for a full copy of the disclaimer.

Analytics provided by The Yield Book® Software.



***An investor should consider the Fund's investment objectives, risks, and charges and expenses carefully before investing or sending any money. This and other important information about the Fund(s) can be found in the Fund's(s) prospectus or summary prospectus which can be obtained at diamond-hill.com or by calling 888.226.5595. Please read the prospectus or summary prospectus carefully before investing. The Diamond Hill Funds are distributed by Foreside Financial Services, LLC. (Member FINRA). Diamond Hill Capital Management, Inc., a registered investment adviser, serves as Investment Adviser to the Diamond Hill Funds and is paid a fee for its services. Like all mutual funds, Diamond Hill Funds are not FDIC insured, may lose value, and have no bank guarantee.***

# Diamond Hill High Yield Fund Commentary

As of March 31, 2019

*All Fund returns based on Class I shares.*

The Fund generated a 6.51% total return during the first quarter compared to 7.40% for the ICE BofA ML U.S. High Yield Index. Since inception on December 4, 2014, the Fund generated an annualized total return of 7.59% compared to 5.43% for the High Yield Index.

The High Yield Index began the year with a yield to worst (YTW) of 7.95% and an option-adjusted spread (OAS) of 533 bps. After generating a 7.40% total return for the quarter, the High Yield Index ended the quarter with a 6.48% YTW and OAS of 405 bps. The strong return for the High Yield Index more than offset the -4.67% return in the fourth quarter of last year. This is another example of the resilience of the high yield asset class. Over the last two quarters, the High Yield Index generated a 2.39% return while the S&P 500 was -1.72% and the Russell 2000 was -8.56%.

We want to hold up better than peers in down markets and then capture our fair share of the upside in strong markets. This should allow us to achieve competitive high yield returns over a complete market cycle. While we typically focus on much longer time periods, the last two quarters are instructive because they represent a mini-cycle over which we tracked our long-term objectives. Our performance compared to peers in the Morningstar High Yield Category was strong in the fourth quarter of last year and then weak in the first quarter of this year. But, over both quarters, the Fund was in the 2nd percentile of the category. Compared to the High Yield Index, the Fund captured only 55% of the downside in the fourth quarter and then 88% of the upside in the first quarter. For the six month period, the Fund generated a positive 3.77% return, which was 138 bps better than the 2.39% return of the High Yield Index. While the beginning of the fourth quarter seemed like a horrible time to invest in high yield, we are pleased with the Fund's absolute return over this six-month period.

## TEAM


**Bill Zox, CFA**
Portfolio Manager

**John McClain, CFA**
Portfolio Manager

**Suken Patel, CFA**
Assistant Portfolio Manager

**Douglas Gimple**
Senior Portfolio Specialist


Last quarter, we wrote about an 18 percentage point increase in the Fund's exposure to BB-rated bonds during 2018 as Treasury yields increased and credit spreads widened. Treasury yields declined and credit spreads narrowed dramatically in the first quarter and BB-rated bonds benefited from both. As the price of BB-rated bonds approached our estimates of intrinsic value, we reduced the Fund's BB weighting by about 7 percentage points and increased the weighting in BBB-rated bonds by about 6 percentage points. High yield investors were moving up in credit quality which made BB-rated bonds more expensive. Investment grade investors were also moving up in credit quality which made certain BBB-rated bonds attractive, particularly compared to BB-rated bonds. In addition, while interest rates remain low, we are, at the margin, willing to bear more interest rate risk relative to credit risk at this stage of the cycle.

The Federal Reserve spent most of 2018 trying to get out of the business of suppressing volatility in financial assets. After risk assets started to buckle in the fourth quarter, the Fed realized that financial conditions were unnecessarily tight and the Fed shifted to a much more dovish stance. While volatility in both bonds and stocks has come down far more than we expected, we are confident that it will come back as is typical later in the economic and market cycles. We want to be in a strong position to take advantage of that volatility. As always, we are focused on delivering competitive high yield returns over a complete market cycle by holding up better during down markets and capturing our fair share of up markets.

## PERIOD AND AVERAGE ANNUAL TOTAL RETURNS AS OF MARCH 31, 2019

| | SINCE INCEPTION (12/4/14) | 3-YR | 1-YR | YTD | 1Q19 | EXPENSE RATIO |
|---|---|---|---|---|---|---|
| RETURNS AT NAV (WITHOUT SALES CHARGE) | | | | | | |
| **Class I** | 7.59% | 9.90% | 7.12% | 6.51% | 6.51% | 0.67% |
| BENCHMARK | | | | | | |
| **ICE BofAML U.S. High Yield Index** | 5.43 | 8.69 | 5.94 | 7.40 | 7.40 | — |

Must be preceded or accompanied by a prospectus.

***Risk Disclosure:*** The value of fixed-income securities varies inversely with interest rates; as interest rates rise, the market value of fixed-income securities will decline. Lower quality debt (i.e.:"High Yield") securities involve greater risk of default or price changes due to potential changes in the issuer's credit quality.

The views expressed are those of the portfolio managers as of March 31, 2019, are subject to change and may differ from the views of other portfolio managers or the firm as a whole. These opinions are not intended to be a forecast of future events, a guarantee of results, or investment advice.

***The performance data quoted represents past performance; past performance does not guarantee future results.*** *The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. The Fund's current performance may be lower or higher than the performance data quoted. Investors may obtain performance information current to the most recent month-end, within 7 business days, at diamond-hill.com.*

The quoted performance for the Fund reflects the past performance of the Diamond Hill High Yield Fund, L.P. (the "High Yield Partnership"), a private fund managed with full investment authority by the fund's Adviser. The Fund is managed in all material respects in a manner equivalent to the management of the predecessor unregistered fund. The assets of the High Yield Partnership were converted into assets of the fund prior to commencement of operation of the fund. The performance of the High Yield Partnership has been restated to reflect the net expenses and maximum applicable sales charge of the fund for its initial years of investment operations. The High Yield Partnership was not registered under the Investment Company Act of 1940 and therefore was not subject to certain investment restrictions imposed by the 1940 Act. If the High Yield Partnership had been registered under the 1940 Act, its performance may have been adversely affected. Performance is measured from December 4, 2014, the inception of the High Yield Partnership and is not the performance of the fund. The assets of the High Yield Partnership were converted, based on their value on December 31, 2015, into assets of the fund prior to commencement of operations of the fund. The High Yield Partnership's past performance is not necessarily an indication of how the fund will perform in the future either before or after taxes.

Performance returns assume reinvestment of all distributions. Returns for periods less than one year are not annualized. Class I shares have no sales charge.

Fund holdings subject to change without notice.

The ICE BofA Merrill Lynch U.S. High Yield Index tracks the performance of U.S. dollar denominated below investment grade corporate debt publicly issued in the U.S. domestic market. This index does not incur fees and expenses (which would lower the return) and is not available for direct investment.

The index data referenced herein is the property of ICE Data Indices, LLC, its affiliates ("ICE Data") and/or its third party suppliers and has been licensed for use by Diamond Hill Capital Management, Inc. ICE Data and its third party suppliers accept no liability in connection with its use. See diamond-hill.com for a full copy of the disclaimer.

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